

LEGAL AND POLICY ANALYSIS | DECEMBER 22, 2019 | AUTHOR: HDEEL ABDELHADY

## U.S. Sanctions on Nord Stream 2 and TurkStream Pipeline Projects (NDAA 2020)

On December 20, 2019, the President signed into law the National Defense Authorization Act for Fiscal Year 2020 (**NDAA**). Title 75 of the NDAA contains the “Protecting Europe’s Energy Security Act of 2019,” which authorizes the President to impose sanctions on foreign persons who knowingly sell, lease, or provide vessels for the construction of the Nord Stream 2 or TurkStream pipeline projects, or any successor to either project. The policies advanced by PEESA are consistent with prior U.S. policy and legislation, particularly the Countering America’s Adversaries Through Sanctions Act of August 2017. This MassPoint publication discusses PEESA’s policies, sanctions mechanics, the relationship between PEESA and CAATSA, and key takeaways.

### Sense of Congress and Policy Objectives

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#### U.S. Support for a Unified Europe; Germany’s Expected Role in Countering Russia With Sanctions

Amidst ongoing challenges to the European Union as an entity and a concept—from Brexit to statements of the U.S. President—the Protecting Europe’s Energy Security Act of 2019 (“**PEESA**” or the “**Act**”)<sup>1</sup> recounts the United States’ historical encouragement and support for the “European project” and hails the “unprecedented prosperity and stability” that it has secured.<sup>2</sup>

PEESA expresses Congress’ sense that the United States’ relationships with Europe and in particular with Germany are “critical” to U.S. national security interests. The Act singles out Germany as a “crucial partner for the United States in multilateral efforts aimed at promoting global prosperity and peace” and for its leadership within the EU and in international fora “to ensure that sanctions imposed with respect to the Russian Federation for its malign activities are maintained.”<sup>3</sup> Implicitly, PEESA conveys Congress’ desire that Germany will maintain Russia sanctions, including those it authorizes as to the Nord Stream 2 and TurkStream pipelines.

#### Reducing Russia’s Control of Natural Gas Transmission to Europe; Continuation of Natural Gas Flows Through Existing Pipelines (Particularly Through Ukraine)

PEESA’s policy objectives specific to Russian natural gas in Europe are articulated in the Act’s provisions governing its termination. Section 7503(h) provides that PEESA will terminate five years after the date of

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<sup>1</sup> Although PEESA is discussed in the body of this publication, statutory citations in footnotes are to the NDAA.

<sup>2</sup> NDAA § 7502(2).

<sup>3</sup> *Id.* at § 7502(3) and (5).

its enactment, unless earlier terminated upon certification by the President to Congress that “appropriate safeguards have been put in place” to:

(A) Minimize the ability of the Government of the Russian Federation to use [Nord Stream 2, TurkStream, or any successor pipeline projects] as a tool of coercion and political leverage, including by achieving the unbundling of energy production and transmission so that entities owned or controlled by that Government do not control the transmission network for the pipeline; and

(B) to ensure, barring unforeseen circumstances, that the project would not result in a decrease of more than 25 percent in the volume of Russian energy exports transiting through existing pipelines in other countries, particularly Ukraine, relative to the average monthly volume of Russian energy exports transiting through such pipelines in 2018.<sup>4</sup>

The provision on unbundling tracks EU energy market policy mandating that “vertically integrated undertakings” “unbundle” ownership and control of natural gas production and transmission, and appears designed to diminish Russian Government ownership and control over natural gas transmission via the Nord Stream 2 pipeline,<sup>5</sup> which is majority owned by Gazprom, a company that is, in turn, majority owned by the Russian Government.<sup>6</sup>

The provision on ensuring that Russian natural gas continues to flow at certain levels through existing pipelines appears aimed at mitigating quantitative and qualitative losses to Ukraine in particular.<sup>7</sup>

## Sanctions Mechanics: Timing of Initial Sanctions, Waivers, Exceptions, and Termination

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### Identification of Vessels Engaged in Pipeline Construction and Sanctionable Foreign Persons; Reports to Congress; Financial and Immigration Sanctions Authorized

Section 7503 of PEESA requires the Secretary of State, acting in consultation with the Secretary of the Treasury, to periodically submit a report to Congress that “identifies”

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<sup>4</sup> The policy objective discernable from § 7503(h)(B) could potentially give rise to collateral legal challenges to PEESA on the grounds that, *inter alia*, the it advances anti-competitive objectives.

<sup>5</sup> The term “‘vertically integrated undertaking’ means a natural gas undertaking or a group of natural gas undertakings where the same person or the same persons are entitled, directly or indirectly, to exercise control, and where the undertaking or group of undertakings perform at least one of the functions of transmission, distribution, LNG or storage, and at least one of the functions of production or supply of natural gas.” Directive 2009/73/EC, Article 2(20). At the WTO, Russia challenged, *inter alia*, unbundling measures contained in Directive 2003/55/EC and implementing measures adopted by Croatia, Hungary, and Lithuania. See, e.g., Tom Miles, [Russia loses bulk of WTO challenge to EU gas pipeline rules](#), Reuters, August 10, 2018 (reporting that “Russia argued that the EU broke WTO rules by requiring the ‘unbundling’ of gas transmission assets and production and supply assets, which effectively stopped Gazprom - long the major supplier of gas to Europe - from owning the pipelines through which it sent gas to the European market.”)

<sup>6</sup> See Gazprom, [share ownership as of December 31, 2018](#).

<sup>7</sup> See, e.g., Dina Khrennikova et al., [Why the Russia-Ukraine Gas Dispute Worries Europe](#), Bloomberg, Dec. 6, 2019 (“Ukraine earns \$3 billion a year from carrying Russian gas to Europe and wants to hang onto the business with a new 10-year agreement for 60 billion cubic meters of annual shipments. Last year, Russian giant Gazprom PJSC sent 87 billion cubic meters -- more than 40% of its exports to Western Europe and Turkey -- via the pipeline network run by Ukraine’s Naftogaz JSC.”).

vessels that engaged in pipe-laying at depths of 100 feet or more below sea level for the construction of the Nord Stream 2 pipeline project, the TurkStream pipeline project, or any project that is a successor to either such project; and

foreign persons . . . [that have been determined to have] knowingly<sup>8</sup> . . . sold, leased, or provided those vessels for the construction of such a project; or

facilitated deceptive or structured transactions to provide those vessels for the construction of such a project.<sup>9</sup>

The Secretary of State's first report must be transmitted to Congress within 60 days of December 20, 2019, the date of PEESA's enactment. Thereafter, reports are due to Congress every 90 days.<sup>10</sup> Although the transmission of reports to Congress is not an express prerequisite for the imposition of sanctions, it is not clear from PEESA's text if the President may impose sanctions prior to the transmission of a report to Congress (and this seems unlikely).<sup>11</sup>

A "foreign person" means a person identified in a report of the Secretary of State and an "individual or entity that is not a United States person."<sup>12</sup> With respect to foreign persons identified in a report of the Secretary of State, the Act authorizes the President, pursuant to the International Emergency Economic Powers Act, to block those foreign persons' property and interests in property that is in the United States, comes within the United States, or is or comes within the possession or control of a natural or legal U.S. person (wherever in the world that U.S. person is located).<sup>13</sup>

In addition, foreign persons identified in a report of the Secretary of State are "inadmissible" to the United States, ineligible to receive visas or other documentation to enter the United States, or to be otherwise admitted or paroled into the United States, or to receive "any other benefit under the Immigration and Nationality Act." In addition, any visa or other U.S. entry document granted to a foreign person identified in a report must be revoked.<sup>14</sup>

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<sup>8</sup> Whether a person acts "knowingly" is assessed by both subjective and objective standards. Under PEESA, "'knowingly', with respect to conduct, a circumstance, or a result, means that a person has actual knowledge, or should have known, of the conduct, the circumstance, or the result." NDAA § 7503(i)(4).

<sup>9</sup> NDAA 7503(a)(1).

<sup>10</sup> *Id.* at § 7503(a)(1) and (a)(2).

<sup>11</sup> As discussed below, PEESA's [provision providing a safe harbor for parties](#) that swiftly undertake good faith wind down efforts suggests that the Act, in at least the case of good faith wind down activities, contemplates reporting to Congress before sanctions are imposed. However, as the wind down provision is specific, it should not be relied on to support a conclusion that prior reporting to Congress is generally required before sanctions may be imposed.

<sup>12</sup> *Id.* at § 7503(b)(2) and § (i)(3). A "United States person" means a U.S. citizen or permanent resident; "an entity organized under the laws of the United States or any jurisdiction within the United States, including a foreign branch of such entity"; and, "any person within the United States." § 7503(i)(5).

<sup>13</sup> *Id.* at § 7503(c). "Interests in property" means property owned 50% or more by one or more sanctioned persons, pursuant to OFAC's "50% Rule." *See, e.g.*, MassPoint PLLC, [OFAC Clarifies: Russia-Ukraine Sectoral Sanctions Prohibitions on "Debt" Apply to Credit Sale and Licensing Transactions](#), May 2, 2019.

<sup>14</sup> *Id.* at § 7503(b).

## Financial Sanctions Safe Harbor For “Good Faith” Wind Down Efforts Made Within 30 Days of December 20, 2019; New OFAC FAQ

PEESA prohibits the President from imposing sanctions

with respect to a person identified in the first report submitted . . . [by the Secretary of State within 60 days of PEESA’s enactment] if the President certifies in the report that the person has, not later than 30 days after . . . [December 20, 2019], engaged in good faith efforts to wind down operations that would otherwise subject the person to the imposition of sanctions.<sup>15</sup>

The Act does not define or elaborate on what constitutes a “good faith” effort to wind down, and administrative interpretation of this and other points requiring clarification will likely be forthcoming as enforcement gets underway.

On December 20, 2019, the Department of the Treasury’s Office of Foreign Assets Control (**OFAC**) published Ukraine/Russia Sanctions FAQ No. 815, in response to PEESA’s enactment. The FAQ states as follows:

Upon signature by the President on December 20, 2019, the provisions of Section 7503 of the NDAA immediately became effective. In order to comply with the wind-down provisions of Section 7503(d) of the NDAA, involved parties that have knowingly sold, leased, or provided vessels that are engaged in pipe laying at depths of 100 feet or more below sea level for the construction of Nord Stream 2 or TurkStream must ensure that such vessels immediately cease construction-related activity. Notwithstanding the above, good-faith wind-down exceptions may be made for the safety of the pipeline or safety and care of the crew aboard the vessel, the protection of human life, or maintenance to avoid any environmental or other significant damage, as further described in Section 7503(e).<sup>16</sup>

### Presidential Discretion to Waive Sanctions

The Act authorizes the President to waive immigration and financial sanctions if the President determines that “waiver is in the national interests of the United States” and the President submits to Congress a report on any waivers and the reasons for such waivers.<sup>17</sup> Because PEESA does not enumerate any circumstances that would justify Presidential waiver or otherwise set waiver standards, the President’s discretion to waive sanctions is broad.

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<sup>15</sup> *Id.* at § 7503(d).

<sup>16</sup> OFAC Ukraine/Russia-related Sanctions FAQ No. 815, [How does the U.S. government plan to implement the wind-down specified in Section 7503\(d\) of the National Defense Authorization Act for Fiscal Year 2020 \(NDAA\), also known as the Protecting Europe’s Energy Security Act of 2019?](#)

<sup>17</sup> NDAA § 7503(f).

## Statutory Sanctions Exceptions for Safety, Repair and Maintenance, and Environmental Remediation

PEESA provides that sanctions “shall not apply” to persons providing services or engaged in services ancillary to the construction or regular operation of the Nord Stream 2 and TurkStream pipelines, or any of their successor projects. Specifically, sanctions “shall not apply” to:

- (1) Persons “providing provisions to a vessel . . . if such provisions are intended for the safety and care of the crew aboard the vessel, the protection of human life aboard the vessel, or the maintenance of the vessel to avoid any environmental or significant damage”; or
- (2) a person “engaging in activities necessary for or related to the repair or maintenance of, or environmental remediation with respect to, a pipeline project.

In addition, PEESA provides sanctions exceptions for “authorized” U.S. intelligence, law enforcement, and national security activities, as well for the admission of otherwise inadmissible foreign persons to comply with the United Nations Headquarters Agreement.<sup>18</sup>

## Termination of Sanctions Authority and Previously Imposed Sanctions

As stated above, the President’s authority to impose sanctions and any sanctions imposed by the President pursuant to PEESA expire five years after the date of PEESA’s enactment, unless earlier terminated after the President makes the certifications to Congress [discussed above](#).<sup>19</sup>

## International Emergency Economic Powers Act Penalties

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PEESA authorizes the President to “exercise all authorities” under the International Emergency Economic Powers Act (IEEPA) to carry out Section 7503.<sup>20</sup> In addition, IEEPA’s civil and criminal penalties apply to persons who violate, attempt or conspire to violate, or cause a violation of Section 7503 “or any regulation, license, or order issued to carry out” Section 7503.<sup>21</sup> Civil penalties under IEEPA are up to the greater of \$250,000 or an amount twice the amount of the “transaction that is the basis of the violation with respect to which the penalty is imposed.” Criminal penalties are a fine of up to \$1,000,000 and/or, in the case of individuals, imprisonment for up to 20 years.<sup>22</sup>

## Relationship to Countering America’s Adversaries Through Sanctions Act

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Legislative authority for U.S. sanctions on persons and activities in support of Russian natural gas pipelines was previously provided by the Countering America’s Adversaries Through Sanctions Act (**CAATSA**), enacted on August 2, 2017. PEESA has in common with CAATSA policy positions and objectives, and both laws authorize sanctions. There are also notable differences between the two laws.

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<sup>18</sup> *Id.* at § 7503(e).

<sup>19</sup> *Id.* at §7503(h).

<sup>20</sup> IEEPA, 50 U.S.C. §§ 1701-1708.

<sup>21</sup> NDAA § 7503(g)(2).

<sup>22</sup> 50 U.S.C. § 1705.

CAATSA authorizes the President to, in his or her discretion, impose sanctions on persons who “knowingly” make an investment “that directly and significantly contributes to the enhancement of the ability of the Russian Federation to construct energy export pipelines” or sell, lease, or provide services “to the Russian Federation for the construction of Russian energy export pipelines, goods and services, technology, information, or support.”<sup>23</sup> PEESA, in contrast, makes the imposition of sanctions mandatory in the absence of a statutory exception, waiver, or certification that a party has engaged in good faith activities to wind down activities within 30 days of PEESA’s enactment. Further, PEESA casts a wider sanctions net than CAATSA insofar as it applies to all foreign persons who sell, lease, or provide vessels for the construction of Nord Stream 2, TurkStream, or any successor to either project, and not just to transactions with, directly benefiting, or more closely tied to the Russian Federation.

Importantly, CAATSA called on the President to coordinate sanctions with U.S. allies; PEESA legislates a unilateral approach by omitting any requirement of multilateral coordination.

Notably, PEESA is less restrictive than CAATSA inasmuch as the Act’s sanctions do not apply to the “importation of goods.”<sup>24</sup>

Finally, PEESA’s policy objectives are consistent with those expressed by Congress in CAATSA, including that it “is the policy of the United States to continue to oppose the Nord Stream 2 pipeline given its detrimental impacts on the European Union’s energy security, gas market development in Central and Eastern Europe, and energy reforms in Ukraine.”<sup>25</sup>

## Key Takeaways

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- PEESA implements through sanctions stated U.S. policy judgments that Russia’s increasing natural gas exports to Europe through the Nord Stream 2 and TurkStream pipelines undermines Europe’s energy security and the national security interests of the United States and Europe, and in particular those of Ukraine.<sup>26</sup>
- PEESA is consistent with the general policies advanced by prior U.S. legislation, namely CAATSA. However, as discussed above, PEESA – which, *e.g.*, limits the President’s sanctions discretion, does not call for sanctions coordination with U.S. allies, and casts a wider sanctions net—is more assertive than CAATSA in its use of sanctions aimed Nord Stream 2 and TurkStream.
- Parties seeking to avoid sanctions by utilizing PEESA’s good faith wind down safe harbor must act very quickly as the safe harbor applies to parties that engage in good faith wind down efforts not later than 30 days after December 20, 2019.

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<sup>23</sup> CAATSA, Pub. L. No. 115–44 (2017) § 232 (codified at 22 U.S.C. § 9526).

<sup>24</sup> NDAA § 7503(e)(5).

<sup>25</sup> CAATSA, Pub. L. No. 115–44 § 257(a)(9); 22 U.S. Code § 9546(a). CAATSA also states that it is U.S. policy, *inter alia*, “to work with European Union member states and European Union institutions to promote energy security through developing diversified and liberalized energy markets that provide diversified sources, suppliers, and routes . . . and . . . prioritize the export of United States energy resources in order to create American jobs, help United States allies and partners, and strengthen United States foreign policy.”

<sup>26</sup> Critics of U.S. policy and the use of sanctions to curb the construction of natural gas export pipelines to Europe argue that the United States’ objective—or animating objective—is to secure a market exports of its own natural gas.

- PEESA does not state expressly that parties who facilitate, *e.g.*, prohibited sale or leasing transactions—such as financial intermediaries, logistics services providers—would potentially be sanctionable only for such activities. It is not clear, for example, if the provision of logistics in support of the sale, lease, or provision of a vessel for construction would constitute the sanctionable “providing” of a vessel under PEESA. That potential ambiguity aside, the Act is clear that non-principal parties to covered transactions and other foreign persons are sanctionable if they “facilitate deceptive or structured transactions to provide” vessels for construction. Therefore, parties should ensure that their activities are not clearly or potentially within PEESA’s grip as to evasive transactions.
- With respect to the safety, environmental, and other sanctions exceptions provided for by PEESA, the key point to note is that these exceptions apply to activities that are *ancillary* to the construction or regular operation of the pipelines. That said, it is likely that interpretive guidance on these matters—as [OFAC’s new FAQ](#) might suggest—will be provided by U.S. authorities, or may be gleaned from future sanctions enforcement actions, license issuances, or other sanctions administration and enforcement actions.<sup>27</sup>
- It should be noted that the Trump Administration has on several recent occasions issued general licenses temporarily authorizing otherwise prohibited and sanctionable activities, such as to facilitate wind down and maintenance transactions in cases where sanctions resulted in harm or market/industry disruptions beyond those intended.<sup>28</sup> Should Nord Stream 2 and TurkStream sanctions create market, foreign policy, or other disruptions beyond those anticipated—particularly in the near term—administrative measures providing temporary and limited authorizations or other relief may follow.

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For more information about this publication and MassPoint Legal and Strategy Advisory PLLC’s related [sanctions counseling and compliance services](#), contact the author, [Hdeel Abdelhady](#).

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<sup>27</sup> As [indicated above](#), OFAC’s new Russia/Ukraine-related Sanctions FAQ in response to the NDAA’s passage appears to put the human life, environmental, and significant damages exceptions as “good-faith wind down” category. These are, as discussed above, statutory exceptions separate from PEESA’s provision prohibiting the imposition of sanctions on persons certified by the President to have made “good faith efforts to wind operations” within 30 days of PEESA’s enactment. NDAA § 7503(d). While the State Department is the agency primarily charged with identifying sanctionable persons, the Treasury Department, through OFAC, will play a significant role and will likely issue additional FAQs or other guidance on PEESA.

<sup>28</sup> For example, licenses granted in relation to Venezuela (*e.g.*, [CITGO-related transactions](#)), Iran (*e.g.*, [COSCO Shipping \(Dalian\)-related transactions](#)), and Russia (*e.g.*, [RUSAL-related transactions](#)).